

Overview of Madison's Property and Sales Taxes

(Assumes Sales Tax Rates as of 1 October 2013)

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Purpose:

This white paper describes both property and sales taxes within the city of Madison and traces them back to the public entity being supported. It is an update to an earlier version of this paper. On 24 June 2013, the Madison City Council passed an additional half cent sales tax to be effective on 1 October 2013. This paper accounts for that increase (first collection due - 20 November 2013).

Madison's municipal services are supported by its General Fund. Overall, about ~12% of each property tax dollar, and less than 28% of each sales tax dollar go to the City's General Fund.

This is not an official Madison City document although every attempt in accuracy has been made.

Overview of Property (Ad Valorem) Taxes: Property owners are familiar with property taxes as they are typically part of a mortgage payment. These taxes are also paid when you get a tag for your car or trailer. Property taxes are collected by the County in which you live and are then distributed to the entity that originated the tax. This could be state, county or municipal governments,

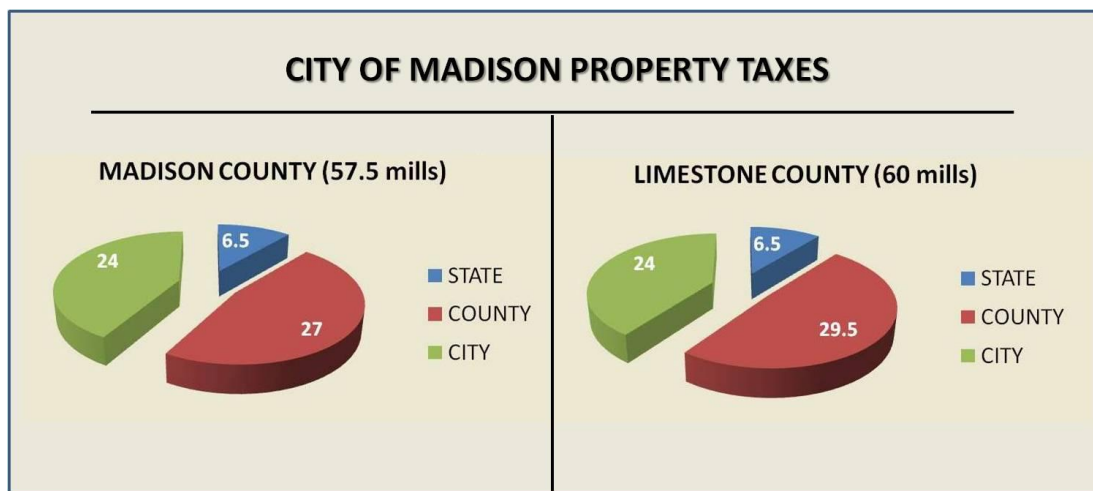


Figure 1 Madison Property Taxes (2013)

school systems, or any other organization managing the funds associated with the millage collected. Figure 1 illustrates that within the City of Madison, a property owner pays either 57.5 mills (Madison County) or 60 mills (Limestone County) depending on the county where the property is located. The difference is because Madison and Limestone Counties have different property tax levies (Limestone's is 2.5 mills more). Property tax levies at the State and City of Madison are the same.

Property taxes must be approved by voter referendum and are based on the assessed value of the property. For personal property, the assessment is 10% of the appraised value (roughly the market

value). On commercial property, the assessment is 20%. For equal valued property, the business owner pays twice the property tax a residential owner would pay.

Property tax is applied to the number of thousands at which a property is assessed. As an example, one would determine the property tax on a home worth \$200,000 as follows¹. You would figure that 10% of the value is 20 thousand dollars. Hence, if your tax rate was 57.5 mills, as it is in Madison County, you would pay 57.5 times 20 (the number of thousands that are taxed): \$1,150. That home in Limestone County would cost the owner \$1,200 (\$50 more). Depending on the county where you live, ~ 40% to 41% of one's property tax (24 mills) payments go back to the City of Madison – the State and County governments get the rest. Dollars coming to Madison City are then split between City Hall, Madison Schools, Madison Utilities (Debt Service) and our Public Library annex.

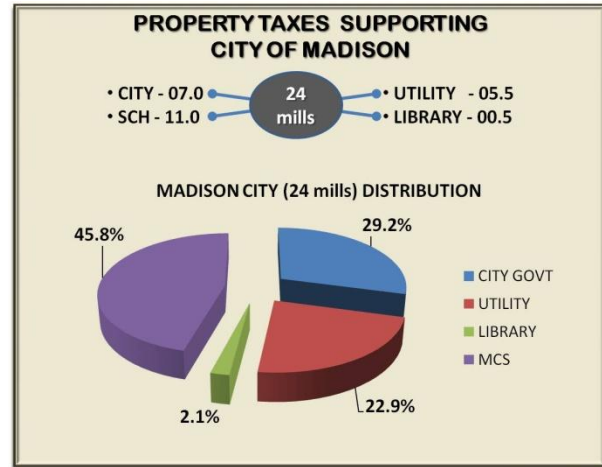


Figure 2 CITY DISTRIBUTION OF PROPERTY TAXES

Figure 2 illustrates what happens to the 24 mills in property taxes collected for the municipal level. **Of the 24 mills taxed, the City government keeps 7 mills** - less than 30% of the 24 mills. Eleven (11) mills go directly to the Madison City School system. The dollars supporting Madison Utility's debt service (5.5 mills) is a result of a 1989 referendum. Our library receives about \$300K / year from its half mill of property tax.

Hence, of the total (57.5 or 60 mills) ad valorem tax dollars paid by Madison property owners, about 12% supports municipal operations. Eighty-eight percent (88%) of our property taxes support state, county and non-municipal local services (schools, utility & library).

Bottom Line: Of each dollar paid in property tax, about 41 cents comes to the City of Madison and of that, only 12 cents go into the general fund for operating the City public safety, infrastructure, recreation and administrative services.

¹ For this paper, no exemptions (Homestead, Old Age, etc) are assumed.

Overview of Sales Taxes:

Over half of Madison's General Fund revenue is generated by sales tax. In a recent report, the Public Affairs Research Council of Alabama (PARCA) provided a breakdown of the income sources for the City of Madison and compared them to other cities in Alabama. For completeness, Huntsville was included. As seen in Figure 3, Madison is very dependent on sales taxes for operational revenue. Data is from 2011.

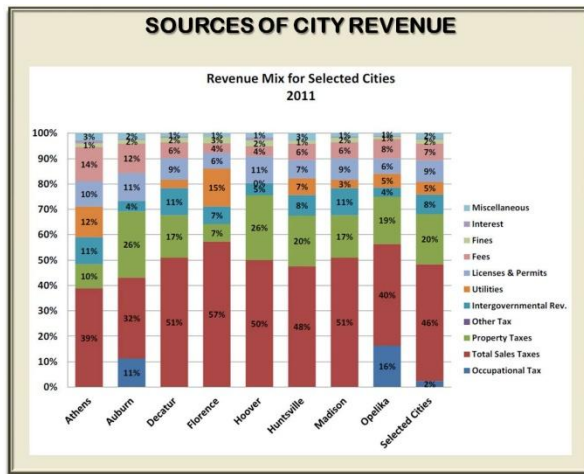


Figure 3 PARCA Revenue Study

Each municipality selected has its unique attributes and circumstances, but it is obvious from this chart that sales taxes are very important to city governments across Alabama. Sales taxes typically generate twice (or more) in revenue than the closest funding stream (normally property taxes). Note that in Auburn and Opelika, there is an occupational tax (city income tax) that is responsible for 11% to 16% of their revenue.

On 24 June 2013, Madison City Council voted to raise our local sales tax by a half-cent effective 1 October 2013. Madison's total sales tax rises to 9.0% in Madison County, and 9.5% in the Limestone portions of the City.

Just like ad valorem taxes, the City of Madison does not receive all the sales tax revenue. The State of Alabama gets 4% of this tax and the County gets 1.5% (in Madison) or 2% (in Limestone). Hence, after 1 October, 3.5% comes to the City of Madison.

It is important to note that not all of the 3.5% is available to the General Fund which is used to operate the city. A half cent (1/2%) goes into the debt service fund which pays various bonds owed by the City. Another half cent goes directly to Madison City Schools to pay their QSCB and BRAC bonds. The Qualified School Construction Bond (QSCB) was used to build James Clemons High School and BRAC bond is funding additional capital improvements to Madison City schools. Hence, 2.5% of the City Sales Tax money goes into the general fund to support the daily operation of our municipal government. See Figure 5.

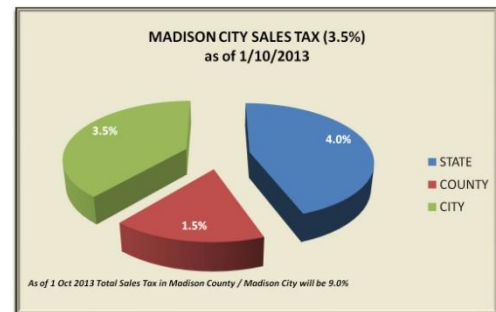


Figure 4 Sales Tax in Madison / Madison County. Note that in Limestone County, the Sales Tax Rate is 2%.

Sales tax revenue reflects our commercial development - having places to shop inside our City limits.

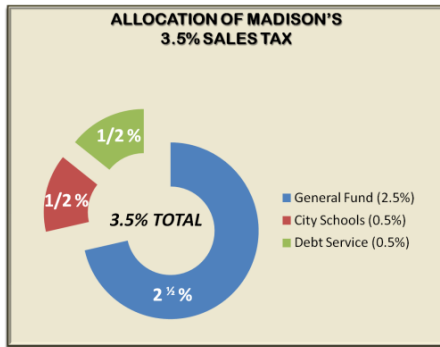


Figure 5 Madison Sales Tax Allocation

Commercial development was not always a top priority in Madison planning, but that is changing. In contrast, Huntsville has focused on commercial development to fund their growth for many years. We can see this whenever we drive down Hwy 72 or I-565. We often shop in Huntsville and not even realize it.

In developing the Madison Growth Plan, the importance of paying much more attention to shopping opportunities for Madison residents inside our city limits was a common theme.

The PARCA study done for Madison mentions that we are in last place, among the cities studied, in terms of sales taxes generated per person. As a local comparison, for every dollar we generate in sales taxes per Madison resident, Huntsville generates over twice that amount per resident. A rule of thumb estimate is that Huntsville generates about \$2.50/person for every dollar in sales tax generated in Madison per person. Ten thousand dollars in sales tax revenue to Madison is approximately \$100,000 to Huntsville as they have 4 times our population. It should be no surprise that Huntsville has a budget over 10 times Madison's to support only 4 times the people – that reflects smart planning and development.

Huntsville's historic attention to commercial development has paid dividends for them over the years. Not only Madison residents, but those from surrounding towns (Athens, Decatur, Triana, Owens Crossroads, etc) and those living in north Alabama counties shop in stores located in Huntsville. While we should not try to be another Huntsville, we must increase our opportunities to shop inside our city limits and build up our economic engine that will allow us to provide the infrastructure and quality of life amenities we expect. We expect our school system to continue to attract new families to Madison and we know property taxes alone will not adequately fund the services needed as we grow. We must expand our sales tax engine through improving our infrastructure and focusing on economic development.

With respect to economic development, my belief is:

1. We must position ourselves to attract the sorts of commercial businesses that will fit into Madison's unique character and not try to be another Huntsville;
2. We must develop the commercial land available inside Madison and maximize its appeal to investors by creating supportive infrastructure (roads, drainage, accessibility to Interstate and highway traffic, etc);
3. We must execute our CIP on schedule to attract commercial business – that means finding the funding to do so, and
4. We must keep our school system and water utility top notch as it is a major factor in attracting and supporting the people to want to live and work in Madison.

For more information – please see my website: www.mike4madison.com